CAPITAL LINK

Moderator: Simos Spyrou
17 November 2020
4:00 p.m. GMT

OPERATOR: This is Conference # 5218927

Operator: Thank you for standing by, ladies and gentlemen, and welcome to the Star Bulk Carriers Conference Call on the Third Quarter and 9-months 2020 Financial Results. We have with us Mr. Pertos Pappas, Chief Executive Officer; Mr. Hamish Norton, President; Mr. Rescos, Chief Operating Officer; Mr. Simos Spyrou; and Mr. Christos Begleris, Co-Chief Financial Officers of the company.

At this time, all participants are in a listen-only mode. There'll be a presentation, followed by a question and answer session. At which time, if you wish to ask a question, please press "star" "1" on your telephone keypad and wait for your name to be announced.

I must advise you that this conference is being recorded today.

I'll now pass the floor to one of your speakers, Mr. Pappas. Please go ahead, sir.

Simos Spyrou: Hi operator, this is Simos Spyrou. Thank you. I'm Simos Spyrou, Co-Chief Financial Officer of Star Bulk Carriers Corp. And I would like to welcome all of you to the Star Bulk Carriers conference call regarding our financial results for the third quarter of 2020.

Before we begin, I kindly ask you to take a moment to read the safe harbor statement on Slide number 2 of our presentation. Today's presentation will focus on an overview of our Q3 results, our cash evolution during the quarter, our operational performance and the industry fundamentals before opening up to questions.

Let us now turn to Slide number 3 of the presentation for a summary of our third quarter 2020 financial highlights. In the 3 months ending September 30, 2020, TCE revenues amounted to $137.8 million, 4.9 percent higher than the $131.3 million for the same period in 2019. Adjusted EBITDA for the third quarter 2020 was $79.7 million versus $72.2 million in third quarter 2019, an increase of 10.4 percent. Adjusted net income for the third quarter amounted to $27.3 million or $0.28 per share versus $17.3 million adjusted net income or $0.18 per share in the third quarter of 2019.

Our time charter equivalent rate during the quarter was $13,083 per vessel per day. Total cash today stands at $225 million with total debt at approximately $1.63 billion pro forma for undrawn liquidity of our working capital facility.

Our strong cash flow generation in the third quarter, in combination with our recent refinancings have increased significantly our liquidity. Until today, we have completed 8 refinancings for 30 vessels, increasing our liquidity by $107 million net of any financing fees. In addition, we have secured commitments, and we are in the process of drawing down funds from 2 financial institutions to refinance an additional 5 vessels, which after prepaying outstanding debt are expected to release net proceeds of approximately $5 million for a total combined benefit of $113 million net of fees.

Slide number 4 graphically illustrates the improvement in the company's cash balance during the third quarter.The company started the quarter with $107.6 million in cash and generated positive cash flow from operating activities of $57 million after including debt proceeds from the financing and repayments, CapEx payments for scrubbers and ballast water treatment systems, we arrived at a healthy cash balance of $222.1 million at the end of the third quarter.

I will now pass the floor to our COO, Nicos Rescos, for an update on our operational performance.

Nicos Rescos: Thank you, Simos. Please turn to Slide number 5, where we summarize our operational performance. OpEx was at $4,244 per vessel per day for the third quarter of 2020. The increase was primarily due to increased forwarding logistics expenses during the quarter to service our fleet. However, we expect OpEx levels to normalize during the fourth quarter. Otherwise, our vessels have operated largely uninterrupted during the third quarter despite the COVID-19 pandemic.

For the 9-month 2020 period, we continue having operating expenses of 13 percent below our listed peer average. Net cash G&A expenses were $985 per vessel per day for the quarter. The combination of our in-house management and the scale of the group enables us to provide our services at very competitive costs, complemented by excellent ship management capabilities. Star Bulk is consistently ranked among the top 5 ship managers evaluated by Rightship, and we currently rank as number 1 among our listed peers.

As of today, we have no remaining drydocking spending for 2020. We are currently operating a fleet of 114 scrubber fitted vessels but on aggregate have already operated consistently for more than 38,000 days.

I will now pass the floor to our CEO, Petros Pappas, for a market update and his closing remarks.

Pertos Pappas: Thank you, Nicos. Please turn to Slide 6 for a brief update of supply. During the first 10 months of 2020, a total of $41.6 million deadweight was delivered and $12.4 million deadweight was sent to demolition for a net fleet growth of 29.2 million deadweight or 3.3 percent. COVID-19 has created strong supply in efficiencies since April with quarantines and crew changes inflating port concession and creating short-term regional shortages of vessels. Given environmental regulations concerning greenhouse gas emissions are expected to keep new building activity under control over the next few years.

The order book has decreased to a record low of 6.3 percent of the fleet with just 9.1 million deadweight firm orders reported by Clarksons year-to-date.

Furthermore, the return of Pakistani breakers, after nearly 2 years of absence, has inflated scrap prices and should make demolition of older tonnage more attractive for shipowners. As a result, we expect net fleet growth to stay below 1.5 percent per annum during the next 3 years.

Despite the strong correction in crude oil prices, the average steaming speed of the dry bulk fleet during the year was down 0.5 percent to approximately 11.5 knots as a result of the IMO low sulfur regulation and the switch to more expensive VLSFO. A recovery of crude oil prices in the medium-term is expected to further incentivize slow steaming and will play a key role for freight rate levels of modern tonnage and may also increase scrubber savings.

Let's now turn to Slide 7 for a brief update of demand. 2020 has been challenging for trade as COVID-19 has affected consumption in the supply chain of all dry bulk cargoes. According to Clarksons, total dry bulk trade during 2020 is estimated to decline by 2.7 percent in tons and 2.3 percent in ton-miles. China has been the driving force of the recovery and has been importing record high volumes of iron ore, soybean and bauxite during the last months. However, economic activity from the rest of the world remains weak with rising concerns on the impact of the second round of lockdowns, especially in Europe.

On a positive note, the availability of a vaccine and a COVID-19 treatment by the end of this year supports an economic rebound during 2021 and 2022. The synchronized global economic stimulus is expected to focus on the construction sector and in face dry bulk trade during the next years. Furthermore, the Brazil iron ore production is gradually recovering from the 2019 Brumadinho dam disaster and will inflate ton-miles over the next few years. During 2021, Clarksons expects dry bulk trade to rebound 3.9 percent in tons and 4.4 percent in ton-miles.

Iron ore ton-miles during 2020 are projected to expand by 1.7 percent. Despite the pandemic, China has produced record high volumes of crude steel since April and raised iron ore imports by 11 percent during the first 10 months of 2020. However, steel production from the rest of the world continues to underperform with September output, down 7 percent year-on-year.

During the third quarter, Brazil iron ore exports increased 11.5 percent last year. And hopefully, this will be the start of a long-term upward trend. Vale has set an annual production target of 400 million tons by 2022 from slightly less than 320 million tons during 2020.

Coal trade has been affected the most from the pandemic this year and is projected to contract 9.9 percent in ton-miles. On top of the strong heating global consumption, China's tension with Australia and supply disruptions in Colombia have had a strong negative effect on vessel requirements with longer distance rates declining the most. During the first 9 months of the year, domestic coal production in China as well as in India increased at a faster pace than thermal electricity and the combination resulted in an increase of stocks and lower import requirements. Having said that, expectations of a colder-than-average winter due to La Ni–a conditions, and the global industrial recovery during 2021 is expected to reverse this trend, creating a favorable short-term outlook for coal trade with 2021 ton-miles projected by Clarksons to rebound 4.7 percent.

Grain and soybean trade during 2020 is projected to increase 5.6 percent in ton-miles. So the back of sharp increase in Latin American soybean exports and a recovery of U.S. exports to China as part of the Phase 1 trade deal. Brazil soybean export season has ended with record high-volume shipped from the country, while U.S. outstanding grain sales stand at record high levels. China's demand for grains is expected to remain strong during the next few years as the next 5-year plan will focus on food security and the hog herd recoveries from the African swine fever.

Minor bulk freight during 2020 is expected to decline by 3.7 percent in ton-miles. However, West Africa bauxite exports continue to expand driven by strong project pipeline generating strong ton-miles for Capesize vessels. The positive effect from the global stimulus should be felt during 2021 and 2022. Clarksons' forecast minor bulk freight to experience a 5.9 percent rebound during 2021.

Finally, as a general comment, the supply-demand balance during the next few years looks bound to tighten and the appropriate conditions are lining up for a sustainable recovery to take place. Q1 and possibly Q2 of next year may be slower for as long as COVID-19 is still prevalent. But once a vaccine and a treatment are mass produced and available, we expect markets to rebound strongly.

Without taking any more of your time, I will now pass the floor over to the operator to answer any questions you may have.

Operator: Thank you very much, sir. Ladies and gentlemen, as a reminder, if you wish to ask a question, please press "star" "1" on your telephone keypad and wait for your name to be announced.

Our first question for today is from Randy Giveans from Jefferies.

Randy Giveans: Well, I guess, first question on the sale-leasebacks and all of the incremental liquidity from that. Can you give us a weighted average interest rate for those deals, just kind of seeing what the cost of financing was?

And then secondly, how does this affect the kind of dividend formula and calculation for your kind of cash balance?

Christos Begleris: Randy, it's Christos. So basically, the average margin of those new financings is in the high 2s. It's around ($275 million), and that's the average for the $500 million of facilities, including the $60 million that we will be drawing in the next few weeks. And effectively, these refinance debt of approximately $390 million, which was priced 20 basis points higher than the new financing. So the interest cost is down on a larger amount. And then the amortization is actually quite lower on the new debt resulting in a usual interest cost for the $500 million, that is $10 million per year lower than what we had on the $390 million that we refinanced.

Randy Giveans: Got it. OK. And then for the dividend calculation now?

Christos Begleris: The dividend calculation is based on, as you know, cash on the balance sheet relative to the number of ships we have, but a lot of the cash on the balance sheet now and perhaps a bit more later, is going to be from refinancing existing ships at higher leverage, where basically, we have the option of counting that cash from refinancing to count toward the dividend or not. To this point, we have opted to basically not count that extra cash as counting towards the dividend. It's possible that management and the Board will change its mind at some point. But I think basically, the intention of that dividend provision was to take into account cash generated from operations.

Randy Giveans: Got it. Yes. I would assume you weren't just borrowing it to pay down the dividend.

Christos Begleris: Right.

Randy Giveans: But I guess, do we just net that off because going into a fourth quarter, you're supposed to earn – or you supposed to have $1.6 million per vessel, and then the incremental cash was to be paid out as a dividend.

Christos Begleris: Correct.

Randy Giveans: So now does that 1.6 number go up? Or do we just take your cash balance and reduce the excess liquidity you got from this refinancing? What's the best way to calc this?

Christos Begleris: I think basically, you should net off the extra cash that we've gotten from the refinancing.

Randy Giveans: Got it.

Christos Begleris: At least for the time being.

Randy Giveans: Yes. That's fair. And then I guess in terms of use of cash is just to build a fortress balance sheet in case there's a very soft market in '21. Are you looking at some fleet renewal, maybe some second-hand acquisitions?

Like where do you see the use of cash and kind of your fleet going forward?

Christos Begleris: Yes. I think for the near term, you should think about this cash as cash on hand in case we have a pandemic. And last I looked, we had a pandemic. So there's more risk in the world, and that was why we wanted to refinance some of our ships to generate some more cash. Obviously, our intention is not to keep large quantities of cash on the balance sheet indefinitely. So we will be using cash for productive purposes.

Randy Giveans: Noted. All right. Well, I have a few more questions, but I'll hop off and let you all go.

Operator: Our next question today is from Ben Nolan from Stifel.

Ben Nolan: Maybe following up on that last one a little bit. Obviously, one of your competitors have been really busy selling assets. And at least historically speaking, they're at pretty low prices relative to, say, average modern asset values. Is that at all interesting to you? Is that something that you're looking at? Or are you thinking of it pretty much as similar to what you've done in the past, if you can get a ship for shares type of a situation and maybe you'll look at it, otherwise, not?

Christos Begleris: I think basically, given where our share price is at this point, a ship for shares transaction could be quite interesting. And basically ships for cash at this point, probably less so.

Ben Nolan: OK. And another thing, I know – and having looked through some of your previous presentations, then – it appears to be pretty pleased with the CCL pool for the Capes and Newcastlemaxes. The – I was curious – well, first of all, assuming that, that's correct, would you – or how do you think about maybe deploying the Kamsarmaxes or Supramaxes or other parts of the portfolio into similar scalable arrangements?

Petros Pappas: Ben, do you mean – this is Petros. Do you mean whether we would form a pool on Kamsarmaxes or Supras?

Ben Nolan: Well, you tell me. I mean it looks like the CCL pool is working out for you? I don't know. Is that something that you would like to apply to rest of the fleet in some form or fashion?

Petros Pappas: Actually, to be honest with you, I think that it makes even more sense to be in a pool for smaller vessels. The reason is the following – when you have a big number of vessels, you have them dispersed all over a certain ocean. And therefore, when new business comes in, you have a bigger probability that you're going to be closer to the loading port. And that actually happens more with smaller vessels, meaning Supras and Panamax, Kamsarmax, then with Capes. Capes have set routes. So you cannot actually get as much of an advantage as you could on the smaller carrier. So it's fun enough, we've been discussing this the last days that formation of a pool on those smaller sizes would be beneficial going forward.

Ben Nolan: OK. Interesting. And then lastly, I don't want to overdo it on the dividend question, but I do think it's important. So should we – again, the calculation has become a little bit more ambiguous. Should we assume that until the market gets better, where there's probably not going to be any dividend payments. Is that sort of the read-through here?

Christos Begleris: That's probably the logical conclusion. I mean a market at this level could lead to a dividend eventually, but a dividend in the near term probably requires a better market.

Ben Nolan: And as part of that...

Christos Begleris: As Petros said, we wouldn't be shocked if we see a better market next year.

Ben Nolan: Sure. And as part of these new financings, there's no restrictions on your ability to pay or anything of that. It's just a decision on your part?

Christos Begleris: Correct. That's correct.

Operator: Our next question is from Amit Mehrotra from Deutsche Bank.

Amit Mehrotra: Sorry, I dialed in quite late actually. So the question – forgive me if this has been answered. But did you guys provide a fourth quarter bookings percentage and rate? And Christos or Simos, I think, with some of the refinancing I gymnastics that you guys have done, I think your breakeven's actually come down from the $11,000 plus level, if you can just give us a finer point on what the breakeven is pro forma for all that stuff that you guys have done?

Petros Pappas: Amit, it's Petros. We have booked about 65 percent of our Q4 at levels of about $13,500 now the 35 percent left, it's probably going to be lower because the market has gone down. Right now, I would say that Ultras are at mid-high 9s, Panamaxes are around $10,500 and Capes around $13,000, $13,500. So I would expect that this $13,500 that we fixed up now may go down to about what we've seen during Q3, unless, of course, if the market. moves up in the last 45 days of the quarter, which I would not rule out. As for the break, I will let...

Amit Mehrotra: Is that on a scrubbed or unscrubbed basis the numbers that you are providing?

Petros Pappas: These are roughly on a scrubbed basis.

Amit Mehrotra: Scrubbed basis. OK. Sorry, go ahead. Yes.

Petros Pappas: Ad for our breakeven, I'll let the CFO take this part of the question.

Christos Begleris: Amit, from my side, it's Christos. So basically, our breakeven or cash breakeven, as you correctly have pointed out, has actually dropped to slightly below $11,000 per day. We are at around $10,900 on a cash basis.

Amit Mehrotra: OK. Great. And then, Hamish, I'm surprised that there's so many questions around dividends because the market is not that great right now. But I wanted to kind of use that as opportunity to revisit the whole strategy behind the dividends. I mean correct me if I'm wrong, but the whole kind of motive behind the dividend was to allow the equity value to trade above NAV, which will give you a currency to delever the balance sheet and then you have basically a delevered kind of dry bulk company, which obviously commensurate very low breakevens. I mean the outlook for the market is incredibly different than when it was a year ago. It's not bad. But it's not the super cycle that we once predicted prior to the COVID crisis as it relates to IMO 2020.

So in that context, I'm just wondering like does the dividend hold as much of a priority in your head or the company's mind that it did this time a year ago in the context of the outlook is better, but it's not necessarily the windfall opportunity that you guys thought it was a year ago or all of thought it was a year ago?

Hamish Norton: No. I think the dividend is just as important as it was. And frankly, I think the opportunity may be better than it was. The opportunity for 2020 was, obviously, that we were going to have a pretty good market without a pandemic, and we were going to have great returns on the scrubbers, which obviously was affected quite substantially by the pandemic.

But going forward, we have a ridiculously low order book. We have a very tiny fleet growth expected next year, well below what we expect to be the growth in the ton-mile demand. And yet, who is going to be brave enough to order a ship next year, right? I mean, if you order a ship next year, you're making a bet on the political acceptability of your fueling choice 5 years out from the date of order, and nobody knows. There's tremendous uncertainty about what sort of ship you're supposed to order and how long that ship will be grandfathered in. So we expect frankly, that the order book will remain very low, even in the face of a pretty good market, which should be a tremendous opportunity.

Amit Mehrotra: OK. And then just related to the scrubber, I mean the scrubber economics are not horrible. They're OK. I mean there's still a spread in terms of high sulfur fuel.

Can you just baseline, where is that spread today? I think it's like $60, $70?

Hamish Norton: It's not $70.

Amit Mehrotra: And obviously, oil prices are coming back higher, jet fuel, diesel distillate demand in general should improve in a post vaccine world. Could it be possible that like the scrubber economics become more compelling, even though they are actually pretty decent now even at $70 spread.

Hamish Norton: Yes, yes. No. Let's put it this way. At $70, it's a decent return on investment. At $150 or $200 or $250, it becomes better than a return on investment. What's crucial is demand for low sulfur refined products. Right now, basically, since there's so little demand for jet fuel and diesel demand is somewhat suppressed, the most profitable low sulfur product of a refinery is low sulfur fuel for ships, which is very unfortunate from the point of view of the scrubber economics.

But once jet fuel demand comes back and diesel demand comes back, it should be quite expensive for the refineries to produce a marginal barrel of low sulfur fuel for ships because the sulfur removal capacity at the refineries will be stretched, which it is not today. So the scrubber economics should come back faster than the increase in oil prices.

Amit Mehrotra: OK. That's interesting. And then the last question I had, if I could. I guess this is for Christos and Simos. You guys decided to put a press release in the press release, the fact that you're compliant with all your covenants, which obviously you are, given the fact that the net debt is coming down at the company. But obviously, like that begs the question of like what is the covenant and how quickly are asset values declining relative to your ability to lower the liabilities of the company?

And so last quarter, you were very helpful in terms of providing where the gross and net LTVs were. I guess the banks maybe look at it on an asset to value basis. I don't know how you look at it internally, but it would be really helpful if you could help us think about what the pro forma value is on a net (gross) basis, especially given there is a seller of assets seemingly at any price to diversify a way into like a random kind of business, but I'd just love to get your perspective on that.

Christos Begleris: So there is a big buffer. The short answer, Amit is that there's a big buffer in the value covenant that we have for our fleet. The corporate covenant that we have right now is at 70 percent, and that's on the basis of basically total debt over total assets, including our cash. The net debt levels that we have for our fleet, which would yield sort of an equivalent ratio to the covenant. Based on the values that we have as of the 30th of September because essentially, those covenants are tested at the last day of each quarter, yields a ratio that is in the mid-50s. Therefore, there is plenty of buffer and room even if any competitor flooded the market and depress further value by a large extent.

Amit Mehrotra: Is that a value that you guys come up with? Or is it an independent appraisal of the asset? Like who comes up with what the value of the asset is at the end of the 90-day period?

Christos Begleris: We wish we would come up with our own valuations but that's best (inaudible). No, it's basically from a pre-selected group of valuers and the likes of Clarksons, Braemar, et cetera, so the big sort of brokerage houses.

Operator: Next up, we have some follow-up questions from Randy Giveans.

Randy Giveans: Just a quick question following up on the hedges, right? You have, I think, 8,000 metric tons remaining in November and December. You had 71,000 tons or so last quarter. So I guess, for 2020, does that mean you haven't added any hedges recently? And then your prior press release stated you had, I think, 24,000 tons in 2021, with your current press release doesn't mention '21. Did you sell those? Or what is the status of those?

Petros Pappas: Correct. We have liquidated those, Randy, when 2021 was at levels below $60 per ton. And this has proved so far, at least, to be a good move, given that right now, 2021, the spread trades at around $80 per ton given also the latest announcements about vaccine and further progress on treatment for COVID.

Randy Giveans: Got it. And then can you help with the – getting to the $2.66 per ton, that is sizable. Were those just locked in at the beginning of the year, and that's just kind of a remaining position?

Petros Pappas: Yes. Those were essentially locked in December 2019, when it was a very different world to where we are today.

Operator: There are no further questions waiting. I'll now hand back to the speakers.

Petros Pappas: Thank you, operator. No more comments from us. Good night, and stay safe.

Operator: Thank you very much, sir. Ladies and gentlemen, that does conclude the call. Thank you everyone for joining. You may now disconnect.

END